No. 87-1841

Supreme Court, U.S.
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In the Supreme Court of the United States

October Term, 1987

CITY OF SANTA MONICA, California,

Petitioner,

v.

SHELL OIL COMPANY,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

CROSS PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Are leases of subsurface municipal lands for private crude oil pipelines subject to judicial review under the Commerce Clause, or are the parties free under the Market Participant Doctrine to seek mutually acceptable terms, where the municipality, as lessor, competes with other public and private entities in the relevant and diverse market?

2. Does the Commerce Clause, in the absence of implementing Congressional action, confer upon private parties the right to permanently occupy the subsurface of city streets for their exclusive proprietary use despite the city's objection?

LIST OF PARTIES

A complete list of parties appears in the Caption and at pages iii - x of the Petition for Writ of Certiorari herein. The City of Santa Monica is a political subdivision of the State of California, operating under a Freeholders Charter.

TOPICAL INDEX

Page

Opinions Below 1

Jurisdiciton 2

Constitutional Provisions Involved 2

Statement Of The Case 3

A. Nature of the Controversy 3
B. Statement of Facts 4
C. Proceedings Below 4

Reasons For Granting The Writ

I

The Decision Of The Court Of Appeals Conflicts With This Court's Market Participant Cases And Raises Questions Unresolved By The Court's 4-4 Affirmance In *Western Oil & Gas Ass'n v. Cory* 5

II

The Decision Of The Court Of Appeals, Suggesting That Santa Monica Must Yield Sovereign Property Where Necessary To Facilitate Interstate Commerce, Raises Important Issues Of Federalism 9

Conclusion 16

TABLE OF AUTHORITIES CITED

Cases	Page
Bibb v. Navajo Freight Lines, 359 U.S. 520 (1959)	11
Block v. North Dakota, 461 U.S. 273 (1983)	13
Commonwealth Edison Co. v. Montana, 453 U.S. 609 (1981)	8, 15
Cooley v. Board of Wardens, 55 U.S. (12 How.) 299 (1851)	11, 12
Detroit United Ry v. City of Detroit, 229 U.S. 39 (1913)	12
Garcia v. San Antonio Metropolitan Transit Authority, 469 U.S. 528 (1985)	10
Golden State Transit Corp. v. City of Los Angeles, 475 U.S. 608 (1986)	13
Gurnsey v. Northern California Power Co., 160 Cal. 699, 117 P. 906 (1911)	7
Harris v. McRae, 448 U.S. 297 (1980)	15
Haskell v. Kansas Natural Gas Co., 224 U.S. 217 (1912)	14
Hughes v. Alexandria Scrap, 426 U.S. 794 (1976)	15
Kansas City Gas Co. v. Kansas City, 198 F. 500, 518 (W.D. Mo. 1912)	14
Kassell v. Consolidated Freightways Corp., 450 U.S. 662 (1982)	11, 12
Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 (1982)	13
Los Angeles Athletic Club v. Board of Harbor Comm'nrs, 130 Cal. App. 376, 20 P.2d 130 (1933)	8
Los Angeles County v. Southern California Tel. Co., 32 Cal.2d 378, 196 P.2d 773 (1948)	7
Maher v. Roe, 432 U.S. 464 (1977)	15
New England Power Co. v. New Hampshire, 455 U.S. 331 (1982)	8

Raymond Motor Transportation, Inc. v. Rice, 434 U.S. 429 (1978) 11
Reeves, Inc. v. Stake, 447 U.S. 429 (1980) 5, 6, 8, 9
San Francisco Street Artists Guild v. Scott, 37 Cal.App.3d 667, 112 Cal. Rptr. 502 (1974) 12
South Carolina v. Baker, ___ U.S. ___, 56 U.S.L.W. 4311 (April 20, 1988) 10
South Central Timber v. Wunnicke, 467 U.S. 82 (1984) 6
St. Louis v. Western Union Tel. Co., 149 U.S. 465 (1893) 12, 13
Sunset Telephone & Telegraph Co. v. City of Pasadena, 161 Cal. 265, 119 P. 796 (1911) 13
West v. Kansas Natural Gas Co., 221 U.S. 229 (1911) 14
Western Oil & Gas Ass'n v. California State Lands Comm'n, 105 Cal. App. 3d 554, 164 Cal. Rptr. 468 (1980) 8
Western Oil & Gas Ass'n v. Cory, 726 F.2d 1340 (9th Cir. 1984), *aff'd per curium by an equally divided court*, 471 U.S. 81 (1985) 5, 6
White v. Mass. Council of Construction Employers, 460 U.S. 204 (1983) 5, 8
Williams Pipe Line Co. v. City of Mounds View, 651 F.Supp. 551 (D.Minn. 1987) 13

Statutes

Public Utilities Code
§6203 7
§6231 7
28 United States Code
§1254(1) 2
49 United States Code
§2001(4) 10

Constitutions

California Constitution
Article XVI, Section 6 7
United States Constitution
Amendment V 13
Amendment X 3
Article 1, Section 8, cl. 3 2

Rules

Supreme Court Rules
Rule 19.5 1
Rule 20.5 1

Other Authorities

Hartman, *State Taxation of Interstate Commerce*, 122 (1953) 8
10 McQuillan, *Municipal Corporations*, §§ 30.39, 30.40 (3d ed. 1981) 7
10 McQuillan, *The Law of Municipal Corporations*, § 30.73, p. 763 (3d ed. 1981) 12-13
Regan, *The Supreme Court and State Protectionism: Making Sense of the Dormant Commerce Clause*, 84 Mich.L.Rev. 1091 (1986) 14

No. _____

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CITY OF SANTA MONICA, California,

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SHELL OIL COMPANY,

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CROSS PETITION FOR WRIT OF CERTIORARI

Pursuant to Supreme Court Rules 19.5 and 20.5, the City of Santa Monica respectfully requests that a Writ of Certiorari be issued to the United States Court of Appeals for the Ninth Circuit to review its Judgment entered on October 21, 1987.[1]

OPINIONS BELOW

The Opinion of the Court of Appeals for the Ninth Circuit is reported at 830 F.2d 1052 (9th Cir. 1987) and

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[1]This Cross-Petition for Writ of Certiorari is filed contemporaneously with the City's Brief in Opposition to (Shell Oil Company's) Petition for Writ of Certiorari. This Cross-Petition is conditional on the grant of Shell's Certiorari Petition.

is reprinted as Appendix A to the Petition for Writ of Certiorari; the Order denying rehearing and rejecting the suggestion for rehearing en banc is reprinted as Appendix C.

The Memorandum of Decision and the Judgment of the District Court for the Central District of California (Honorable Robert J. Kelleher, presiding) are not reported; they are reproduced as Appendices B and D to the Petition for Writ of Certiorari.[2]

JURISDICTION

The Opinion of the Court of Appeals for the Ninth Circuit was issued on October 21, 1987; Judgment was entered the same date.

A timely petition for rehearing, filed by Shell Oil Company, was denied by Order entered on January 11, 1988.

This Cross-Petition is filed pursuant to Supreme Court Rule 19.5. A Petition for Writ of Certiorari by Shell Oil Company was docketed in this Court and received by Cross-Petitioner on April 11, 1988.

The Court has jurisdiction of the Cross-Petition pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISIONS INVOLVED

This case involves construction of the Commerce Clause and the Tenth Amendment of the United States Constitution.

1. U.S. Const., Art. I, § 8, cl. 3 states:

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[2]Appendix (App.) citations are to the Appendix to (Shell Oil Company's) Petition for Writ of Certiorari.

> The Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.

2. U.S. Const., Amend. X states:

> The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.

STATEMENT OF THE CASE

A. Nature of the Controversy.

This is an action under the Commerce Clause. Shell's complaint contends that the Clause, in its dormant state, requires that Santa Monica grant Shell a perpetual lease of the subsurface of city streets for Shell's private exclusive use. It further claims a right to such lease for a nominal fee, not to exceed the City's costs and any loss resulting from the grant. In contrast, the City does not believe the Commerce Clause was intended to confer such rights, tantamount to eminent domain, on private parties. Moreover, even if the Clause could in some cases require affirmative governmental action in aid of commerce, the City is exempt from scrutiny here since it is but one of many participants in the relevant market.

Both in its sovereign and proprietary capacities, Santa Monica asserts the right to determine whether and on what terms to grant leases to private parties. The City has proposed a fee based on the fair rental value of an exclusive subsurface easement. Any amount less than that would be contrary to the City's fiduciary responsibilities.

The judgment of the Court of Appeals, while upholding the City's mechanism for setting rental fees,

nonetheless suggests requirements for local governments which are inconsistent with the Commerce Clause and principles of federalism. The notion that private firms may appropriate permanent exclusive rights in municipal property (whether the governmental interest is proprietary or sovereign) is both novel and important. No less disturbing is the prospect of a wide range of municipal contracts having to be submitted to federal courts for approval.[3]

B. Statement of Facts

The City incorporates by reference the Statement of Facts in its Brief in Opposition to the Petition for Writ of Certiorari.

C. Proceedings Below.

The City incorporates by reference the statement of Proceedings Below in its Brief in Opposition to the Petition for Writ of Certiorari.

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[3]Shell's Complaint sought: (1) a declaratory judgment regarding the permissible terms for a new franchise; and (2) a permanent injunction "requiring defendant City to grant Shell all necessary rights required to allow Shell to continue to transport crude oil by said pipeline through the City conditioned on the payment of a fee as determined by the Court. . . ." CR 1:10.

REASONS FOR GRANTING THE WRIT

I

THE DECISION OF THE COURT OF APPEALS CONFLICTS WITH THIS COURT'S MARKET PARTICIPANT CASES AND RAISES QUESTIONS UNRESOLVED BY THE COURT'S 4-4 AFFIRMANCE IN *WESTERN OIL & GAS ASS'N v. CORY*

This case is the sequel to *Western Oil & Gas Association v. Cory*, 726 F.2d 1340 (9th Cir. 1984). The Ninth Circuit's decision in that case, rejecting the market participant doctrine[4] in reviewing pipeline easements over state coastal lands, was affirmed by an equally divided Court. 471 U.S. 81 (1985) (Powell, J., not participating). The Court of Appeals found that case controlling, although "the present case is distinguishable from *Cory*." App. A-9.

The prevailing rule is that "state proprietary functions are exempt from Commerce Clause scrutiny." *Reeves, Inc. v. Stake*, 447 U.S. 429, 437 n.9 (1980). The threshold question is "whether a particular state action more closely resembles an attempt to impede trade among private parties, or an attempt . . . to govern the State's own economic conduct and to determine the parties with whom it will deal." *White*, 460 U.S. at 218 (1983) (Blackmun, J., concurring in part). Here, the District Court answered that question in favor of market participant status. It found the parties' relationship was contractual, not regulatory; Shell's lease was the subject

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[4]"[S]tate and local governments are [not] restrained by the Commerce Clause when they seek to effect commercial transactions not as 'regulators' but as 'market participants.' " *White v. Mass. Council of Construction Employers*, 460 U.S. 204, 206 (1983).

of "arms length negotiation between parties of equal bargaining power." App. B-8.

This Court has noted three exceptions to the market participant doctrine, foreign commerce, natural resources, and restrictions on resale, *South Central Timber v. Wunnicke*, 467 U.S. 82, 96 (1984), none of which are applicable here. In *Cory*, the Ninth Circuit created two more exceptions, monopoly market position, and property held in a sovereign capacity. 726 F.2d at 1343. The first is consistent with the doctrinal basis for market participant immunity; state participation in, rather than regulatory control over, the market.[5] However, the second exception found by the court, and prominent in its decision here, is wholly inconsistent with the doctrine.

Santa Monica does not enjoy monopoly power, as did the State in *Cory*. This was the finding of the District Court on undisputed evidence. CR 78:95, 129, 215; 96:5; 80:24. Accordingly, the Court of Appeals rested its holding on its "sovereign capacity" exception. App. A-9-10. The court reasoned that when the city enters the market with land it holds in a sovereign capacity, rather than with property "purchased or acquired by the city through its entry into the real estate market," App. A-11 n.5, it is not engaged in "marketplace conduct." *Id.*

The decision of the Court of Appeals fails to recognize that state proprietary functions are not incompatible with sovereign powers. A state may exercise both authorities with respect to the same property. *Reeves,*

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[5] As explained in *Reeves*, where the state has "unique access" to the commodity being traded, such as scarce natural resources, the prospect of economic Balkanization is more problematic. 447 U.S. at 444.

447 U.S. at 439 n.12 ("[w]hen a State buys or sells, it has the attributes of both a political entity and a private business"). That Santa Monica may have acquired its property interest in the subsurface of the streets in its political capacity does not foreclose it from subsequently exercising proprietary powers.[6] A city's authority over municipal property may be described as "sovereign" when examining the breadth of its power. Thus, characterization of a city's interest in its streets as "sovereign" is usually made in the context of determining the scope of municipal authority or autonomy from state control. *See generally* 10 McQuillan, *Municipal Corporations*, §§ 30.39, 30.40 (3d ed. 1981). At the same time, a city may act as a private trader when dealing with persons seeking to acquire a commercial interest in that property.[7]

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[6]California authorizes its charter cities to act in a proprietary manner in the leasing of municipal property for non-public utility pipelines. *See e.g.*, Cal. Public Utilities Code § 6203 (city may grant franchise upon "terms and conditions . . . whether governmental or contractual in character, as in the judgment of the legislative body are to the public interest"); *id.* § 6231 (franchisee shall pay "an annual franchise fee in an amount agreed to by the applicant and the municipality").

[7]Shell argues that the City has no proprietary interests itself in subsurface property, but it may nonetheless grant such interests to third parties. It is not immediately obvious how the City might do this. If it only exercises sovereign authority, as trustee of public rights and interests, the City surely cannot allow permanent and exclusive private use. Cal. Const. Art. XVI, Section 6 (prohibiting gifts of public property); *Los Angeles County v. Southern California Tel. Co.*, 32 Cal.2d 378, 196 P.2d 773, 780 (1948) (street franchise to public utility violates state constitutional prohibition if it fails to confer sufficient public benefit). Thus, Shell's argument proves too much, because it would require Shell to obtain subsurface rights from each of the individual land owners along the route. *See Gurnsey v. Northern California Power Co.*, 160 Cal. 699, 117 P. 906 (1911).

It is the relationship between the state and commerce which determines whether the Commerce Clause applies, not whether the state acts in a "sovereign capacity" in other respects. *New England Power Co. v. New Hampshire*, 455 U.S. 331, 338-39 n.6 (1982) (market participant exemption depends on whether state is regulating use, not on manner of ownership of its property). Thus, the "single inquiry" in this case is whether the particular conduct under challenge constitutes "state participation in the market." *Reeves*, 447 U.S. at 436 n.7; *White*, 460 U.S. at 208. That sovereign interests may be simultaneously at work, does not defeat the market participant doctrine.

Accordingly, sovereign ownership of land does not preclude government from exercising proprietary control. *Western Oil & Gas Ass'n v. California State Lands Comm'n,* 105 Cal. App. 3d 554, 566, 164 Cal. Rptr. 468, 475 (1980) ("[w]hen the state leases trust lands, it is exercising a proprietary function");[8] *Los Angeles Athletic Club v. Board of Harbor Comm'nrs*, 130 Cal. App. 376, 386, 20 P.2d 130, 134 (1933) (lease of public trust lands is a proprietary, not governmental, function). Indeed, the Court of Appeals' rejection of Santa Monica's proprietary interest in municipal property is inconsistent with its contemporaneous holding that lease rent constitutes a "user fee." *See Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 622 n.12 (1981) (" 'user' fees 'partake of the nature of a rent charged by the State, based upon its proprietary interest in its public property' ") (citing P. Hartman, *State Taxation of Interstate Commerce*, 122 (1953)).

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[8]The cited case resolved the state issues in *Cory*, upon abstention by the District Court.

The inadequacy of the Court of Appeals' revision to the market participant doctrine is well illustrated by the instant case. Santa Monica exercises control over Shell's subsurface pipeline only to the extent specified in a freely negotiated lease; no more than any private landowner. For the City to benefit from the lease, it must not bargain so hard as to motivate Shell, its only customer[9], to utilize alternatives available to it. The City is thus constrained by the free market in dealing with Shell. Santa Monica's interest, like that of any private trader, is to get fair value for use of its property, not to impede trade or secure advantage for domestic commerce.

The "sovereign capacity" exception created by the Court of Appeals is inconsistent with this Court's market participant cases.[10] Because it raises an important and recurring issue, review is warranted.

II

THE DECISION OF THE COURT OF APPEALS, SUGGESTING THAT SANTA MONICA MUST YIELD SOVEREIGN PROPERTY WHERE NECESSARY TO FACILITATE INTERSTATE COMMERCE, RAISES IMPORTANT ISSUES OF FEDERALISM

Shell claims that Santa Monica has no option but to lease city streets to firms engaged in commerce.

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[9]Rather than Santa Monica being a monopolist, Shell is a monopsonist, since it is the only private user of subsurface municipal land. App. A-12, B-6.

[10]Indeed, sovereign ownership would seem to support, not undermine, use of the market participant doctrine. *Reeves*, 447 U.S. at 438 ("[r]estraint in this area is also counseled by considerations of state sovereignty, the role of each State 'as guardian and trustee for its people' ").

Indeed, by its own characterization of the issue, Shell uses the dormant Commerce Clause to compel the City to "surrender" property rights.[11] The Court of Appeals implicitly accepted the claim by suggesting that a decision not to award a franchise would be subject to Commerce Clause scrutiny.[12] If the court is correct in its conclusion that "this case involves lands held in a sovereign capacity," App. A-10, forcing the City to yield proprietary interests in such lands raises serious federalism concerns.

States, in the exercise of sovereign prerogatives, might ordinarily find their basic protection in the "structure of the federal system" rather than in judicial enforcement of Tenth Amendment constraints. *Garcia v. San Antonio Metropolitan Transit Authority*, 469 U.S. 528, 551 (1985). More recently, this Court emphasized in *South Carolina v. Baker*, ___ U.S. ___, 56 U.S.L.W. 4311 (April 20, 1988), that the political process itself is the principal guarantor of structural federalism. But the instant case involves no affirmative expression of federal policy or congressional oversight.[13] Because Shell's demand for proprietary rights in sovereign state property is made to the judiciary, not Congress, the structural safeguards that were critical in *Garcia* and *Baker* are absent here.

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[11]See Cert. Pet. at 6; CR 1:10; "Issues Presented For Review," Appellant's Opening Brief in the Court of Appeals at 1.

[12]The court stated "in deciding *whether*, or on what terms, to grant a franchise for the use of public streets the city may not burden interstate commerce in a manner that violates the dormant Commerce Clause." App. A-11 (emphasis added).

[13]Indeed, Congress has rejected exercising any authority regarding the routing of crude oil pipelines. See 49 U.S.C. § 2001(4) (Hazardous Liquid Pipeline Safety Act) ("this chapter does not authorize the Secretary [of Transportation] to prescribe the location or the routing of any pipeline facility").

The core question is whether the Commerce Clause, by its own force, has divested the States of power to control the disposition of sovereign property. It does to some extent where that property has been dedicated to traditional public transportation uses; a classic focus of the nation-unifying theme of the Commerce Clause. *Cooley v. Board of Wardens*, 55 U.S. (12 How.) 299 (1851).[14] The rule is inappropriate, however, where State property has not been so dedicated, and is instead sought for permanent proprietary use. Thus, it is incorrect to equate, as did the Court of Appeals, common and transient surface street uses with the greatly different character of the subsurface use here.

The Court of Appeals held, as a matter of law,[15] that the lands beneath city streets were "recognized transportation corridors for commerce." App. A-10. But Shell's use of the subsurface differs in material respects from the surface uses that characterize typical transportation cases. It is permanent, rather than transient; it is exclusive, rather than common; and it is private, rather than public. In short, Shell has enjoyed, for the past 47 years, an exclusive proprietary use of city land. And by denying the City's right of reverter, it seeks to transmute its leasehold into a fee.

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[14]However, state autonomy over local transportation facilities will be respected, despite adverse affects on commerce, where regulations advance legitimate local interests, such as safety. *Kassell v. Consolidated Freightways Corp.*, 450 U.S. 662, 670 (1981); *Raymond Motor Transportation, Inc. v. Rice*, 434 U.S. 429, 449 (1978) (Blackmun, J. concurring); *Bibb v. Navajo Freight Lines*, 359 U.S. 520, 523-24 (1959) (with respect to highways, a "state has exceptional scope for the exercise of its regulatory power").

[15]There were no findings below to support the court's conclusion.

The nature of Shell's use, perhaps more importantly than its location below the surface, sets it apart from *Cooley*, *Kassell*, and similar transportation cases. Whether Shell lays its pipeline down the center of Main Street, or five feet beneath it, the line is permanently and exclusively occupying land, not sharing a "transportation corridor."[16]

It makes no difference whether Shell is selling artifacts (*San Francisco Street Artists Guild v. Scott*, 37 Cal. App. 3d 667, 670, 112 Cal. Rptr. 502, 504 (1974)), operating a street railway (*Detroit United Ry v. City of Detroit*, 229 U.S. 39 (1913)), or a telegraph system (*St. Louis v. Western Union Tel. Co.*, 149 U.S. 465 (1893)), it has no right to appropriate city streets without permission.

> "[A]ppropriation of [city streets] to private individual uses, from which the public derive no benefit or accommodation, is a perversion of them from their lawful purposes, contrary to the trust imposed in the city authorities. Thus, it is frequently stated that there is no natural right to use the streets for purposes of private business or gain. And it follows as a corollary that the city may forbid any such use. This is a cardinal doctrine of municipal law." 10 McQuillan, *The Law of Municipal*

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[16] Moreover, Santa Monica is not providing a transportation facility; it is providing bare land. It is Shell that owns and operates the transportation facility, albeit not one that is open to the public. Perhaps this explains why common carrier crude oil pipelines, but not proprietary lines, have rights of eminent domain and are regulated in the public interest.

Corporations, §30.73, p. 763 (3d ed. 1981).[17]

It is another matter altogether when Congress grants federal franchises which require use of city streets. *St. Louis v. Western Union Telegraph Co.*, 148 U.S. 92 (1892). But federal franchisees still have to pay for the space in the streets thus exclusively appropriated. *Id.* at 98-101. Even Congressional preemption of franchise terms "does not require a city to renew or to refuse to renew any particular franchise." *Golden State Transit Corp. v. City of Los Angeles*, 475 U.S. 608, 619 (1986). *Accord Williams Pipe Line Co. v. City of Mounds View*, 651 F.Supp. 551, 569 (D.Minn. 1987) (despite extensive federal regulation, "[c]ounty was at no time required to give a hazardous liquid pipeline company the right to lay its line on county property").[18]

By controlling regular street uses, a state has considerable power over the channels of commerce; a power which can be misused for protectionist purposes. The Commerce Clause interposes the federal judiciary between such parochial interests and the nation's interest

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[17]California follows this "cardinal doctrine." *Sunset Telephone & Telegraph Co. v. City of Pasadena*, 161 Cal. 265, 271, 119 P. 796, 798 (1911) (no right to permanently occupy portions of public highways).

[18]If Congress were to require Santa Monica to grant a proprietary franchise to Shell, it might not raise federalism concerns, but it would require just compensation under the Fifth Amendment. *See Block v. North Dakota*, 461 U.S. 273, 291 (1983). The permanent nature of Shell's physical occupation constitutes a *per se* possessory taking. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982). *Accord, St Louis v. Western Union Telegraph Co.*, 148 U.S. at 100-101.

in free trade.[19] But, while streets are unique and indispensable with respect to transient surface uses, they are fungible with other property in their subsurface uses, as is shown by Shell's easements with many public and private landowners.[20] Unlike the "transportation corridor" setting described by the Court of Appeals, this case does not involve discriminatory or burdensome regulations directed at commerce; indeed, it involves no regulations at all.[21]

Shell claims that denial of a lease would force it to find alternative routes at a higher cost. Cert. Pet. at 4. In essence, it views the Commerce Clause as guaranteeing the lowest cost for doing business. Whether

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[19]The primary purpose of the dormant Commerce Clause has been and should be to prevent states from engaging in purposeful economic protectionism. Regan, *The Supreme Court and State Protectionism: Making Sense of the Dormant Commerce Clause*, 84 Mich.L.Rev. 1091 (1986).

[20]Shell concedes that it frequently obtains subsurface easements from private parties and does so for other portions of the Ventura line. CR 78:156, 167-69.

[21]This case is thus distinguishable from *West v. Kansas Natural Gas Co.*, 221 U.S. 229 (1911), cited by the court as authority for requiring Santa Monica to issue a franchise. There, this Court invalidated a state law prohibiting natural gas pipeline easements across state highways. However, the key ingredient was not the use of highways, but the state's designation of those of its highways which formed state lines as absolute barriers to commerce. As was explained in a later appeal of *West*, the law was integral to a state scheme to prevent the exportation of natural gas. *Haskell v. Kansas Natural Gas Co.*, 224 U.S. 217, 221 (1912). *See also Kansas City Gas Co. v. Kansas City*, 198 F. 500, 518 (W.D. Mo. 1912) ("the purpose of the law after all, masked as it was, contemplated solely and chiefly the prevention of the exportation of gas from the state").

Notably, in these cases, the Court did not consider the "extent of the rights of public or private ownership [of highways] in the State of Oklahoma." *Haskell* at 221.

the claim is protective of shareholders, employees, or consumers, it is misplaced. *Commonwealth Edison v. Montana*, 453 U.S. at 619 ("Commerce Clause [does not give] residents of one State a right of access at 'reasonable' prices to resources located in another State").

This case thus reduces to whether the dormant Commerce Clause requires a state to "surrender" property rights for the private economic benefit of a company engaged in commerce. The "novelty" of the case is Shell's characterization of a possible denial of lease rights "as a burden which the Commerce Clause was intended to make suspect." *Hughes v. Alexandria Scrap*, 426 U.S. 794, 807 (1976). As with fundamental rights analysis under the due process clause,[22] Shell may not claim a constitutional entitlement to governmental benefits which might assist it in carrying on its commercial activities. Just as the "Due Process clause . . . does not confer an entitlement to such funds as may be necessary to realize all the advantages of that freedom," *Harris v. McRae*, 448 U.S. 297, 317-18 (1980), neither does the Commerce Clause confer an entitlement to government property.

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[22]In other contexts, this Court has recognized a sharp distinction between state action burdening the exercise of protected rights and a state's refusal to facilitate their exercise. *See, e.g., Maher v. Roe*, 432 U.S. 464 (1977).

CONCLUSION

For the foregoing reasons, it is respectfully requested that, in the event the Petition for Writ of Certiorari is granted, the Court grant this Cross-Petition as well.

Dated: May 9, 1988

Respectfully submitted,

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PROOF OF SERVICE BY MAIL

State of California

ss.

County of Los Angeles

I, the undersigned, say: I am and was at all times herein mentioned, a citizen of the United States and a resident of the County of Los Angeles, over the age of eighteen (18) years and not a party to the within action or proceeding; that my business address is 11333 Iowa Avenue, Los Angeles, California 90025; that on May 9, 1988, I served the within *Cross Petition for Writ of Certiorari* in said action or proceeding by depositing true copies thereof, enclosed in a sealed envelope with postage thereon fully prepaid, in the United States mail at Los Angeles, California, addressed as follows:

Clerk, United States
Supreme Court
One First Street, N.W.
Washington, D.C. 20543
(Original and forty copies)

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All parties required to be served have been served. I declare under penalty of perjury that the foregoing is true and correct. Executed on May 9, 1988, at Los Angeles, California.

Siri Ved K. Khalsa
(Original signed)